Industrial Bank Conference

Presented by

Department of Financial Institutions

Donald R. Meyer, Commissioner

November 14, 2000

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State of California Business, Transportation and Housing Agency Gray Davis, Governor Maria Contreras-Sweet, Secretary

Welcome and Opening Remarks

Donald R. Meyer Commissioner of Financial Institutions

David L. Scott
Chief State Examiner

Legal Summary - SB 2148

Presented by:

Kenneth Sayre-Peterson Senior Counsel

SB 2148

- Signed by Governor Davis on 9/29/00 Effective on 9/30/00
- Changes name of industrial loan companies to industrial banks
- Makes industrial banks subject to the Banking Law
- Permits industrial banks to engage in all activities of commercial banks, including engaging in the trust business

SB2148 - General provisions

- Definitions now include industrial banks
- Articles of Incorporation requirements purpose clause
- Dividend provisions
- Other Provisions

Chapter 11 - Industrial Banks

- Added to Division 1 of the Financial Code (Banking Law)
- Commencing with Section 1400 Provides that Chapter 11 is a continuation, simplification, recodification of licensing and regulation of deposit taking industrial banks

Significant Financial Code Sections Now Applicable to Industrial Banks

Presented by:

Craig Carlson and Doug Kirkpatrick

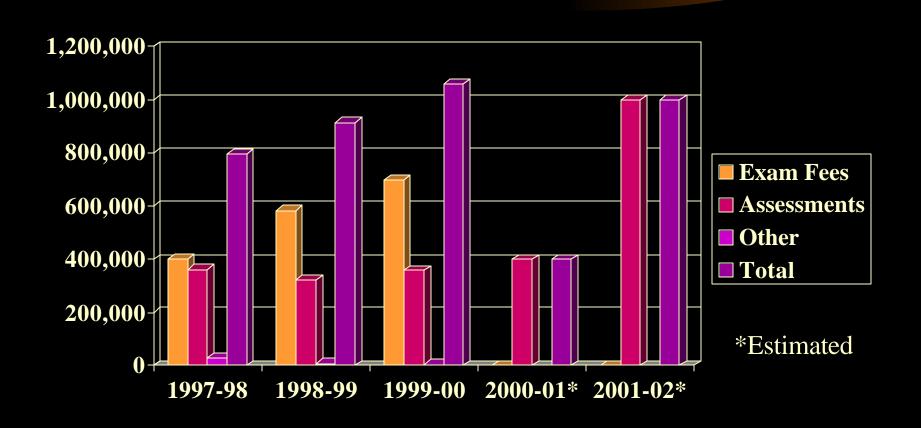
Article 1 - General Provisions

- Section 1402 Separate Fund Account known as Industrial Bank Account
- Section 1403 Annual Assessment Basis -\$5,000 minimum. Now sliding scale - used to be pro-rata based on TA.
- Base rate fixed by the commissioner but shall not exceed \$2.20 per \$1,000 of TA

Assessment Rates

TA (% of Base Millions) A	ssessment Rate
First \$2	100.0
Next \$18	50.0
Next \$80	12.0
Next \$100	6.25
Next \$1,000	6.0
Next \$4,000	3.5
Next \$14,000	3.0
Next \$20,000	2.5
Excess over \$40,000	1.5

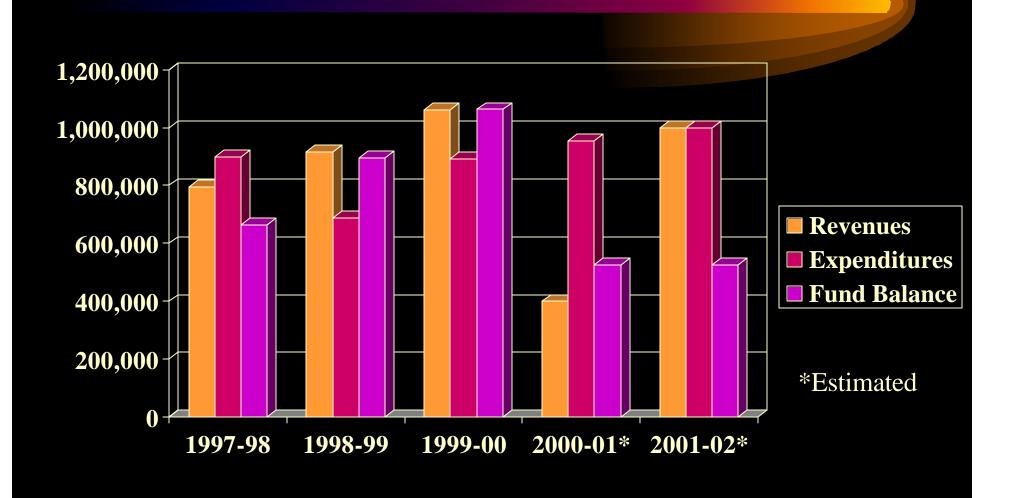
Revenue Sources



Interim Assessment Plan

- Reduce fund balance by \$535,000
- Assess \$400,000 based on new formula on 11/30/00
- Give credit for exam fees paid in current fiscal year up to assessment amount

Industrial Bank Fund



Assessment Comparisons

- Example \$100 million TA
- Biannual Examination Costs \$31,000
- Annual Assessment \$4,500
- Annual Costs \$20,000
- New assessment formula \$25,000
- Assumes \$1.23 assessment rate for 2001-02

Article 2 - Business of Industrial Banks

- Section 1410 Must be FDIC insured while conducting industrial banking business
- Section 1411 May accept deposits which are redeemable prior to stated maturity but may not accept demand deposits
- Section 1412 Other provisions of the division apply as if it were a commercial bank

Section 1412 - Other Provisions

- Chapter 4 (Branch Offices, Other Places of Business and Automated Teller Machines/Begin Sec. 490)
- Chapter 5 (Corporate Requirements/Begin Sec. 600)
- Chapter 6 (Powers and Miscellaneous Provisions/Begin Sec. 750)
- Chapter 6.5 (Agency Activities/Begin Sec. 800)
- Chapter 7 (Deposits/Begin Sec.850)
- Chapter 8 (Withdrawals and Collections/Begin Sec. 952)
- Chapter 10 (Commercial Banks/Begin Sec. 1200)

Other Provisions (cont.)

- Chapter 12 (Trust Companies/Begin Sec. 1500)
- Chapter 13 (Safe Deposits/Begin Sec. 1650)
- Chapter 15 (Examination and Reports/Begin Sec. 1900)
- Chapter 17 (Liquidation, Conservatorship, Reorganization, and Dissolution/Begin Sec. 3100)
- Chapter 18 (Prohibited Practices and Penalties/Begin Sec. 3350)
- Chapter 20 (Bank Extraordinary Situation Closing/Begin Sec. 3600)

Other Provisions (cont....)

- Chapter 21 (Bank Holding Companies/Begin Sec. 3700)
- Chapter 21.5 (Interstate Acquisitions/Begin Sec. 3750)
- Chapter 22 (Foreign (Other State) Banks/Begin Sec. 3800)
- Division 1.5 (Depository Corporations-Sale, Merger, and Conversion/Begin Sec. 4800)

Chapter 4 - Offices and ATMs

- Section 490 Exempts from application process the establishment or relocation of branch or place of business Does not apply to relocation of head office
- Camel 1 and 2 rated banks only otherwise application required
- Regulations CCR 10.6000 10.11876
- Activities of loan production offices
- ATM sections Parity regulations (CCR 10.19601) No notice required

Chapter 5 - Corporate Requirements

- Articles of Incorporation, bylaws and amendments, name changes
- Distribution to Shareholders Restrictions
- Director provisions
- Adequacy of Shareholders Equity Section 660 -Qualitative measures - No statutory capital
- Sale of Securities Stock permit applications
- Acquisition of Control Provisions

Chapter 6 - Miscellaneous Powers/Provisions

- Section 763 Depositaries
- Real property investment provisions
- Conducting of certain activities authorized
- Investing in certain corporations authorized
 - Section 772 (Regs CCR 10.19050 et seq.)
- Extensions of offices Section 776

Chapter 6.5 - Agency Activities

• Covers agency activity requirements for affiliated institutions when acting as either principal or agent.

Chapter 7 - Deposits

- No approvals or restrictions concentrations reviewed for safety and soundness at exam.
- Section 858 Requires that overdrafts over
 90 days be charged off
- Section 864 Set off requirements
- Delayed Funds Availability Policy Same requirements

Chapter 8 - Withdrawals and Collections

• Requirements for certified checks

Chapter 10 - Commercial Banks

- One of the key chapters
- Borrowings and hypothecation of assets Sections 1200 1206
- Loan Limits Sections 1220 1239
- Investments Sections 1335 1338

Borrowing limitations

- Permissible only under conditions specified
- Hypothecation of assets as security for monies borrowed shall not exceed in value the amount borrowed by more than 50% without approval
- Borrowings cannot exceed 100% of shareholders equity without Commissioner approval
- Borrowings from FRB and FHLB permitted
- Securities sold under repurchase agreements are considered borrowings

- Section 1220 (a) Obligations Aggregation rules primarily and secondarily
- Section 1220 (b) Obligations of a person include loans made to others for the benefit of the person.
- Sections 1220 (c) (g) Describe other obligations

- Section 1221 (a) Unsecured limits are 15% of the sum of shareholders equity, allowance for loan and losses and capital notes and debentures.
- Section 1221 (b) Secured and unsecured limits are 25% of the sum of shareholders' equity, allowance for loan losses and capital notes and debentures.

- Section 1223 Loans secured by personal property if not declared ineligible and 15% margin over amount of loan, except bank deposits.
- Section 1223 Loans secured by real property if collateral and obligation conform to Sections 1227, 1228, 1236, 1238, 1239 and first sentence of 1235.

- Ineligible personal property
- Real property secured requirements First lien on real property or leasehold
- "Proper Appraisal"
- Acceptable terms:
 - (a) 10 years flat, LTV < 60%
 - (b) Monthly amortization, maximum 30 year term,<90% LTV
 - (c) Conformance with Civil Code Section 1916.12 Variable Rate Loans

- Acceptable terms (cont..)
 - (d) Farm loans maximum 30 year term, annual amortization, <90% LTV
 - (e) 6 months flat, LTV <85%
 - (f) 60 months flat, LTV <85%, real estate construction loans with plan for repayment or refinancing

Other provisions

- May issue letters of credit and accept drafts or bills of lading
- May make certain loans secured by stock
- Secured and unsecured loans must be separate notes
- Loans exempt from lending limits SBA guaranteed loans, etc

Investments

- Sections 1335 1338
- No real change in investment authority except in Section 772 procedures
- Regulations CCR 10.19050

Chapter 12 - Trust Powers

- Application required Regs CCR 10.3700 10.3861
- Business Plan
- Articles of Incorporation amendment required
- Deposits with State Treasurer

Chapter 13

• Contains requirements and restrictions for safe deposit activities

Chapter 15 - Examinations and Reports

- Article 1. Examinations
- Article 2. Reports
- Article 3. Accounting

Article 1. Examinations

- Section 1900 Statutory examination requirement once every two calendar years
- Section 1901 If "Extra" exam required during same period \$75 per hour, per examiner. If travel outside state necessary examiner travel expenses paid by licensee

Article 1. Examinations

- Section 1902 Annual audited financial statements required prior to 3/31 of each year. Regulations adopted (CCR 10.19401) and no filing with DFI necessary but must be available for review or for filing if requested.
- Other sections Authorizes Commissioner to employ CPAs and appraisers and to examine National banks operating in this state.

Article 1. Examinations

- Section 1912, 1913, 1913.5 Enforcement Actions Corrective action orders and removal/suspension orders provisions
- Sections 1914 1917 Miscellaneous provisions

Article 2. Reports

- Section 1930 covers call reports.
- Section 1934 authorizes special reports as determined necessary by the Commissioner
- Section 1939 requires copies to DFI of certain reports submitted to FDIC and FRB
- Section 1945 requires notification of change in managing officer (CEO)

Article 3. Accounting

- Section 1951 Requires charge-off of any debt due with interest overdue one year unless well secured or in process of collection
- Section 1952 Authorizes Commissioner to require write down of any asset to fair market value

Chapter 17 - Liquidation, Conservatorship, Reorganization and Dissolution

Section 3100 - Covers provisions under which the Commissioner may take possession of a bank. Among other things, if tangible shareholders' equity is less than the greater of 3% of total assets or \$1,000,000

Chapter 17 - Liquidation, Conservatorship, Reorganization and Dissolution

Violations of articles or of law, unsafe or unauthorized conduct of business, failure to pay obligations, unsafe or unsound conditions or failure to comply with any order issued under Section 1913 are also grounds

Chapter 17 - Liquidation, Conservatorship, Reorganization and Dissolution

Section 3150 - Voluntary Liquidation Procedures

Chapter 18 - Prohibited Practices

- Section 3354 Purchases of real or personal property including leaseholds from a subject person requires prior Commissioner approval. FMV standards.
- Section 3355 Purchases of any of the banks assets by subject persons must be not less than fair market

Chapter 18 - Prohibited Practices

- Section 3356 If purchases of any of the banks assets are for less than book value, board must approve by resolution, copy of which submitted to the Commissioner
- <u>Subject Person</u> means any officer or director of the bank, any controlling person of the bank or any officer or director of the controlling person of the bank

Chapter 18 - Prohibited Practices

- Section 3359 Prohibits lending upon own bank stock as collateral. Permits acquisition of shares to prevent loss or if approved by the Commissioner
- Section 3372 Adopts Regulation O Loans to insiders with some modifications
- Regs CCR 10.19300

Other Chapters

- Chapter 20 Bank Extraordinary Situation Closing
- Chapter 21 Bank Holding Companies
- Chapter 21.5 Interstate Acquisitions
- Chapter 22 Foreign (Other State) Banks

Division 1.5

- Sections 4800 4966
- Contains provisions covering procedures and application requirements for sale, merger, conversion of partial or whole business units to and from Federal Depository Corporations.

Conclusions

- Industrial Banks have generally same powers and authority as commercial banks except for demand deposits
- Detailed framework of law and regulations replaced by overall safety and soundness framework
- Parent companies are not subject to the Bank Holding Company Act

Regulatory Expectations

- Strategic Plan Revisions
- Loan Policy Revisions
- Asset-Liability Management Policy Revisions
- Insider Policies Lending and other
- Training and Education

Handout Materials

- Interagency Biographical and Financial Report (for new officers and directors)
- Forms 25 Uniform California
 Application/Notice & Instruction
- Form 510- Depositaries
- Form 700- Application For Specific Authorization to Invest in Corporation (w/Instructions)

Handout Materials

- Form 702 Report of Investment In Corporation (w/Instructions)
- Form 704 Agreement (w/Instructions)
- Form 706 Appointment of Commissioner As Agent for Service of Process (w/Instructions)
- Listing of Ineligible Collateral
- Interagency Statement Branch Names

Questions and Answers

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